

**Initial Statement of Reasons for
Proposed Adoption of California Code of Regulations,
Title 18, Section 1566.1, *Auto Auctions and Auto Dismantlers***

SPECIFIC PURPOSE, PROBLEM INTENDED TO BE ADDRESSED, NECESSITY,
AND ANTICIPATED BENEFITS

Current Law

Sales and Use Tax

California imposes sales tax on retailers for the privilege of selling tangible personal property at retail. (Rev. & Tax. Code, § 6051.) Unless an exemption or exclusion applies, the tax is measured by a retailer's gross receipts from the retail sale of tangible personal property in California. (Rev. & Tax. Code, §§ 6012, 6051.) Although sales tax is imposed on retailers, retailers may collect sales tax reimbursement from their customers if their contracts of sale so provide. (Civ. Code, § 1656.1; Cal. Code Regs., tit. 18, § 1700.)

In general, when sales tax does not apply, California use tax applies to the use of any tangible personal property purchased from a retailer for storage, use, or other consumption and stored, used, or consumed in this state. (Rev. & Tax. Code, § 6201; Cal. Code Regs., tit. 18, § 1620, subd. (b).) The use tax is measured by the sales price of tangible personal property and the person actually storing, using, or otherwise consuming the tangible personal property is liable for the tax. (Rev. & Tax. Code, §§ 6011, 6201, 6202; Cal. Code Regs., tit. 18, § 1685.) However, every retailer "engaged in business" in California that makes sales subject to California use tax is required to collect the use tax from its customers and remit it to the State Board of Equalization (Board), and such retailers are liable for California use tax that they fail to collect from their customers and remit to the Board. (Rev. & Tax. Code, §§ 6202, 6203; Cal. Code Regs., tit. 18, §§ 1684, 1686.)

A "retail sale" or "sale at retail" is a sale of tangible personal property for any purpose other than resale in the regular course of business. (Rev. & Tax. Code, § 6007.) As relevant here, the term "retailer" includes every seller who makes any retail sale or sales of tangible personal property, including sales at auction, and every person engaged in the business of making sales, including sales at auction, for storage, use, or other consumption. (Rev. & Tax. Code, § 6015.)

Sales for Resale

If a person is purchasing property for the purpose of reselling the property in the regular course of business and prior to any storage, use, or other consumption of the property (other than retention, demonstration, or display), the seller may accept a resale certificate

from the purchaser. (Rev. & Tax. Code, §§ 6091, 6092, 6093, 6241, 6242, 6243; Cal. Code Regs., tit. 18, § 1668.) Timely acceptance of a resale certificate in good faith relieves the seller of the liability for the sales tax and the duty of collecting the use tax. (Rev. & Tax. Code, §§ 6092, 6242; Cal. Code Regs., tit. 18, § 1668.)

Each resale certificate must contain provisions required by statute and “be substantially in such form” as the Board shall prescribe. (Rev. & Tax. Code, §§ 6093, 6243.) “In the absence of evidence to the contrary, a seller will be presumed to have taken a resale certificate in good faith if the resale certificate contains essential elements and otherwise appears to be valid on its face. If the purchaser insists that he or she is buying for resale property of a kind not normally resold in the purchaser’s business, the seller should require a resale certificate containing a statement that the specific property is being purchased for resale in the regular course of business.” (Cal. Code Regs., tit. 18, § 1668, subd. (c).)

After issuing a resale certificate in good faith, the purchaser is then generally liable for the sales tax on the subsequent retail sale of the property in California (unless the retail sale is exempt for some other reason). If a purchaser who issues a resale certificate in good faith thereafter makes any use of the property other than retention, demonstration, or display while holding it for resale in the regular course of business, before making a subsequent retail sale of the property, then the purchaser becomes liable for the use tax on the cost of the property. (Rev. & Tax. Code, §§ 6094, 6244; Cal. Code Regs., tit. 18, § 1668, subd. (g).) However, if a purchaser issues a resale certificate for property which the purchaser knows at the time of purchase is not to be resold in the regular course of business, then the purchaser is liable for the sales tax on that purchase measured by the gross receipts from the sale to that purchaser. (Rev. & Tax. Code, § 6094.5; Cal. Code Regs., tit. 18, § 1668, subd. (g).)

Mobilehomes, Commercial Coaches, and Vehicles

In general, every person making a retail sale of a mobilehome, commercial coach, or vehicle is a retailer. However, when the retailer is not licensed or certificated pursuant to the Health and Safety Code (HSC) or Vehicle Code (VC) as a manufacturer, remanufacturer, dealer, dismantler, or lessor-retailer, the use tax rather than the sales tax applies to the sale. The purchaser of the mobilehome, commercial coach, or vehicle is required to pay the use tax to the Department of Housing and Community Development or to the Department of Motor Vehicles at the time of making application for registration or identification. (Cal. Code Regs., tit. 18, §§ 1610, 1610.2.)

Assembly Bill No. 2618

Assembly Bill No. 2618 (Stats. 2012, ch. 756) (AB 2618) added section 6092.5 to the Revenue and Taxation Code (RTC) effective September 29, 2012. RTC section 6092.5 provides that:

- (a) Every qualified person making any sale of a mobilehome or commercial coach required to be registered annually under the Health and

Safety Code, or of a vehicle required to be registered under the Vehicle Code or subject to identification under Division 16.5 (commencing with Section 38000) of the Vehicle Code, or a vehicle that qualifies under the permanent trailer identification plate program pursuant to subdivision (a) of Section 5014.1 of the Vehicle Code, or of any salvage certificate vehicle as defined in Section 11515 of the Vehicle Code, is presumed to be making a sale at retail and not a sale for resale. The presumption may be rebutted by taking a resale certificate from any of the following: (1) A person that certifies it is licensed, registered, regulated, or certificated under the Health and Safety Code or the Vehicle Code as a dealer or dismantler. (2) A person that certifies it is licensed, registered, regulated, or certificated under the Business and Professions Code as an automotive repair dealer, or is qualified as a scrap metal processor as described in the Vehicle Code. (3) A person that certifies it is licensed, registered, regulated, certificated, or otherwise authorized by another state, country, or jurisdiction to do business as a dealer, dismantler, automotive repairer, or scrap metal processor.

(b) A qualified person shall not accept a resale certificate from any person except as provided in subdivision (a).

(c) (1) In addition to the requirements of Sections 6093 and 6243, the certificate shall include the license or registration number of the dealer, dismantler, or automotive repair dealer, as applicable. If the purchaser is not required to hold a seller's permit because the purchaser makes no sales in this state, the purchaser must include on the certificate a sufficient explanation as to the reason the purchaser is not required to hold a California seller's permit in lieu of the seller's permit number. The certificate issued by a purchaser pursuant to this section shall be substantially in such form as the board may prescribe. (2) A qualified person that does not timely obtain a resale certificate as provided in this section may use alternative methods as prescribed by the board to rebut the presumption provided in subdivision (a).

(d) For the purposes of this section, a "qualified person" means a person making a sale at auction or a dismantler licensed under the Vehicle Code.

The July 3, 2012, Senate Floor Analysis of AB 2618 explains that the addition of section 6092.5 to the RTC was intended to address a significant issue regarding "who may purchase salvage vehicles without being required to pay the sales and use tax." The analysis explains further that by creating the presumption that tax applies to sales of specified vehicles by persons at auctions and licensed dismantlers and only permitting such persons to accept resale certificates from persons who certify that they are licensed, registered, regulated, certificated, or otherwise authorized dealers, dismantlers, automotive repairers, or scrap metal processors, AB 2618 "mitigates a significant opportunity to avoid the sales and use tax."

Specific Purpose of, Problems Intend to be Addressed by, Necessity for, and Anticipated Benefits from the Proposed Regulation

Although California Code of Regulations, title 18, section (Regulation) 1668, *Sales for Resale*, provides general guidance regarding the issuance of resale certificates, there is currently no regulation that incorporates the presumption established by RTC section 6092.5, and prescribes the form of the resale certificate that may be taken and the alternative methods that may be used to rebut the presumption in accordance with RTC section 6092.5, subdivision (c). Also, there is no regulation that specifically prescribes the circumstances under which a resale certificate is timely taken in good faith for purposes of rebutting the presumption established by RTC section 6092.5. And, there is no regulation that specifically provides notice regarding a purchaser's tax liability when: (1) property is purchased with a resale certificate prescribed in accordance with RTC section 6092.5, subdivision (c), and the purchaser subsequently makes any storage, use, or other consumption of the property, other than retention, demonstration, or display while holding it for resale in the regular course of business; or (2) the purchaser issues a resale certificate prescribed in accordance with RTC section 6092.5, subdivision (c), for property which the purchaser knows at the time of purchase is not to be resold in the regular course of business.

Board staff held a meeting with interested parties on January 8, 2013, to discuss a draft of proposed Regulation 1566.1, *Auto Auctions and Auto Dismantlers*. The specific purpose of proposed Regulation 1566.1 is to implement, interpret, and make specific the provisions of RTC section 6092.5 and Regulation 1566.1 is intended to specifically address the issues (or problems) identified above.

At the January 8, 2013, meeting, staff responded to written comments received prior to the meeting, as well as other suggestions to add clarifying language to the draft regulation, revise language in the draft regulation to be consistent with RTC section 6092.5, and make some minor grammatical edits. Then, staff incorporated the suggestions discussed at the meeting into a revised draft of the proposed regulation and, on January 10, 2013, staff distributed the revised draft of the proposed regulation to the interested parties that attended the January 8, 2013, meeting and the interested parties that submitted written comments regarding the initial draft of the proposed regulation. However, staff did not receive any comments regarding the revised draft of the proposed regulation from the interested parties.

Therefore, Board staff subsequently prepared Formal Issue Paper 13-003, which recommended that the Board adopt staff's revised draft of Regulation 1566.1 to implement, interpret, and make specific the presumption established by RTC section 6092.5, subdivision (a), and prescribe the form of the resale certificate that may be taken and the alternative methods that may be used to rebut the presumption in accordance with RTC section 6092.5, subdivision (c). Specifically, proposed Regulation 1566.1:

- Specifies that it is presumed that a sale of a “vehicle” by a “qualified person” is a sale at retail and not a sale for resale;
- Identifies those sellers affected by the presumption by defining “qualified person” to mean a person making a sale at auction or a dismantler licensed under the VC;
- Identifies the types of property to which the presumption applies by defining the term “vehicle” to mean: (1) a mobilehome or commercial coach required to be registered annually under the HSC; (2) a vehicle required to be registered under the VC or subject to identification under division 16.5 (commencing with § 38000) of the VC; (3) a vehicle that qualifies under the permanent trailer identification plate program pursuant to subdivision (a) of VC section 5014.1; and (4) any salvage certificate vehicle as defined in VC section 11515;
- Explains that a qualified person may rebut the presumption that its sales of vehicles are at retail, by timely taking in good faith a resale certificate from a person that is: (1) licensed, registered, regulated, or certificated under the HSC or VC as a dealer or dismantler; (2) licensed, registered, regulated, or certificated under the BPC as an automotive repair dealer or is qualified as a scrap metal processor as described in the VC; or (3) licensed, registered, regulated, certificated, or otherwise authorized by another state, country, or jurisdiction to do business as a dealer, dismantler, automotive repairer, or scrap metal processor;
- Provides that a “qualified person” may not accept a resale certificate from any person other than those specified in the regulation;
- Explains when a resale certificate is considered timely taken in good faith in a manner that is consistent with the current provisions of Regulation 1668;
- Describes the essential elements required on a document in order for the document to be considered a resale certificate for purposes of RTC section 6092.5, including the purchaser’s license or registration number, as applicable;
- Prescribes the form of the resale certificate that a “qualified person” may accept and provides that the resale certificate should be in substantially the same form as the resale certificate shown in Appendix A of the proposed regulation;
- Prescribes the alternative methods that may be used to rebut the presumption in RTC section 6092.5; and
- Provides notice regarding a purchaser’s tax liability, under existing law, when property is purchased with a resale certificate, and: (1) the purchaser subsequently makes any storage, use, or other consumption of the property, other than retention, demonstration, or display while holding it for resale in the regular course of business; or (2) the purchaser knows at the time of purchase that the property is not to be resold in the regular course of business.

The Board considered Formal Issue Paper 13-003 during its Business Taxes Committee meeting on March 12, 2013. The Board agreed with staff’s recommendation to adopt staff’s revised draft of Regulation 1566.1 and unanimously voted to propose the adoption of the regulation because the Board determined that the regulation is reasonably necessary to generally address the issues (or problems) identified above. The Board also determined that the adoption of the regulation is reasonably necessary to specifically

implement, interpret, and make specific the presumption established by RTC section 6092.5, subdivision (a), and prescribe the form of the resale certificate that may be taken and the alternative methods that may be used to rebut the presumption in accordance with RTC section 6092.5, subdivision (c). The Board further determined that the regulation is reasonably necessary to specifically provide notice regarding a purchaser's tax liability when property is purchased with a resale certificate prescribed in accordance with RTC section 6092.5, subdivision (c), and: (1) the purchaser subsequently makes any storage, use, or other consumption of the property, other than retention, demonstration, or display while holding it for resale in the regular course of business; or (2) the purchaser knows at the time of purchase that the property is not to be resold in the regular course of business.

The Board anticipates that the adoption of proposed Regulation 1566.1 will benefit the public, including regulated persons, by:

- Providing guidance about and promoting awareness of the presumption established by RTC section 6092.5, and the requirements to rebut the presumption;
- Implementing RTC section 6092.5, subdivision (c)(1) by prescribing the form of the resale certificate that qualified persons may timely take in good faith to rebut the presumption that their sales are at retail;
- Implementing RTC section 6092.5, subdivision (c)(2) by prescribing the alternative methods that qualified persons may use to rebut the presumption that their sales are at retail; and
- Generally helping to mitigate the "significant opportunity to avoid the sales and use tax" identified in the July 3, 2012, Senate Floor Analysis of AB 2618.

The adoption of proposed Regulation 1566.1 is not mandated by federal law or regulations. There is no previously adopted or amended federal regulation that is identical to proposed Regulation 1566.1.

DOCUMENTS RELIED UPON

The Board relied upon Formal Issue Paper 13-003, the exhibits to the issue paper, and the comments made during the Board's discussion of the issue paper during its March 12, 2013, Business Taxes Committee meeting in deciding to propose the adoption of Regulation 1566.1 described above.

ALTERNATIVES CONSIDERED

The Board considered whether to begin the formal rulemaking process to adopt proposed Regulation 1566.1 at this time or, alternatively, whether to take no action at this time. The Board decided to begin the formal rulemaking process to adopt the proposed regulation at this time because the Board determined that the proposed regulation is reasonably necessary for the reasons set forth above.

The Board did not reject any reasonable alternative to proposed Regulation 1566.1 that would lessen any adverse impact the proposed action may have on small business or that would be less burdensome and equally effective in achieving the purposes of the proposed action. No reasonable alternative has been identified and brought to the Board's attention that would lessen any adverse impact the proposed action may have on small business, be more effective in carrying out the purposes for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

**INFORMATION REQUIRED BY GOVERNMENT CODE SECTION 11346.2,
SUBDIVISION (b)(6) AND ECONOMIC IMPACT ANALYSIS REQUIRED BY
GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b)**

AB 2618 added section 6092.5 to the RTC effective September 29, 2012. The Board is proposing to adopt Regulation 1566.1 to implement, interpret, and make specific the presumption established by RTC section 6092.5, subdivision (a), and prescribe the form of the resale certificate that may be taken and the alternative methods that may be used to rebut the presumption in accordance with RTC section 6092.5, subdivision (c). The Board is also including provisions in proposed Regulation 1566.1 to explain when a resale certificate is considered timely taken in good faith that are consistent with the current provisions of Regulation 1668. And, the Board is including provisions in proposed Regulation 1566.1 that provide notice regarding a purchaser's tax liability, under existing law, when property is purchased with a resale certificate, and: (1) the purchaser subsequently makes any storage, use, or other consumption of the property, other than retention, demonstration, or display while holding it for resale in the regular course of business; or (2) the purchaser knows at the time of purchase that the property is not to be resold in the regular course of business.

The Board anticipates that the adoption of proposed Regulation 1566.1 will benefit the public, including regulated persons, by:

- Providing guidance about and promoting awareness of the presumption established by RTC section 6092.5, and the requirements to rebut the presumption;
- Implementing RTC section 6092.5, subdivision (c)(1) by prescribing the form of the resale certificate that qualified persons may timely take in good faith to rebut the presumption that their sales are at retail;
- Implementing RTC section 6092.5, subdivision (c)(2) by prescribing the alternative methods that qualified persons may use to rebut the presumption that their sales are at retail; and
- Generally helping to mitigate the "significant opportunity to avoid the sales and use tax" identified in the July 3, 2012, Senate Floor Analysis of AB 2618.

Therefore, the Board has determined that the adoption of proposed Regulation 1566.1 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California.

In addition, proposed Regulation 1566.1 will not regulate the health and welfare of California residents, worker safety, or the state's environment. Therefore, the Board has also determined that the adoption of proposed Regulation 1566.1 will not affect the health and welfare of California residents, worker safety, or the state's environment.

The forgoing information also provides the factual basis for the Board's initial determination that the adoption of proposed Regulation 1566.1 will not have a significant adverse economic impact on business.

The proposed regulation may affect small business.